

**STATE OF WASHINGTON
OFFICE OF THE INSURANCE
COMMISSIONER**



FINANCIAL EXAMINATION

of

**Enumclaw Property & Casualty Insurance Company
Enumclaw, Washington**

**NAIC CODE 11232
DECEMBER 31, 2004**

**Participating States:
Washington**

**Exhibit A
Order No. G06-19
Enumclaw Property & Casualty
Insurance Company**

SALUTATION

Seattle, Washington
March 31, 2006

The Honorable Alfred E. Gross
Insurance Commissioner
Chair, NAIC Financial Condition (E) Committee
Virginia Bureau of Insurance
Commonwealth of Virginia
PO Box 1157
Richmond, VA 23219

The Honorable Gary Smith
Director, Idaho Department of Insurance
NAIC Secretary, Western Zone
Department of Insurance
700 West State Street
Boise, ID 83720-0043

The Honorable Mike Kreidler, Commissioner
Washington Office of the Insurance Commissioner (OIC)
Insurance Building
302-14th Avenue SW
Olympia, WA 98504

Dear Commissioners and Director:

In accordance with your instructions, and in compliance with the statutory requirements of RCW 48.03.010, an examination was made of the corporate affairs and financial records of

Enumclaw Property & Casualty Insurance Company


of

Enumclaw, Washington

hereinafter referred to as "EPC" or the "Company," at the location of its home office, 1460 Wells Street, Enumclaw, Washington 98022. This report is respectfully submitted showing the condition of the Company as of December 31, 2004.

CHIEF EXAMINER'S AFFIDAVIT

I hereby certify I have read the attached Report of the Financial Examination of Enumclaw Property & Casualty Insurance Company of Enumclaw, Washington. This report shows the financial condition and related corporate matters as of December 31, 2004.



PATRICK H. MCNAUGHTON

Chief Examiner

March 31, 2006

Date

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SCOPE OF THE EXAMINATION

This examination covers the period from the date of incorporation, November 27, 2001 through December 31, 2004 and comprises a comprehensive review of the books and records of the Company. The examination followed the statutory requirements contained in the Washington Administrative Code (WAC), the Revised Code of Washington (RCW), and the guidelines recommended by the National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook (FCEH). The examination included identification and disposition of material transactions and events occurring subsequent to the date of examination that were noted during the examination.

Corporate records, external reference materials, and various aspects of the Company's operating procedures and financial records were reviewed and tested during the course of this examination and are commented upon in the following sections of this report. In addition, the Company's certified public accountant's (CPA's) work papers were reviewed and utilized, where possible, to facilitate efficiency in the examination.

INSTRUCTIONS

The examiners reviewed the Company's filed 2004 NAIC Annual Statement as part of the statutory examination. This review was performed to determine if the Company completed the NAIC Annual Statement in accordance with the NAIC Annual Statement Instructions and to determine if the Company's accounts and records were prepared and maintained in accordance with Title 48 RCW, Title 284 WAC, and the NAIC Statements of Statutory Accounting Principles (SSAP) as contained in the NAIC Accounting Practices and Procedures Manual (AP&P).

The following summarizes the exceptions noted while performing this review.

1) NAIC Annual Statement Errors and Misclassifications

The results of the examination disclosed several instances in which the Company's filing of the 2004 NAIC Annual Statement did not conform to the NAIC Accounting Practices and Procedures Manual and the NAIC Annual Statement Instructions. While the Company needs to correct these practices, none of the following items in the instruction were material to the financial statements and no examination adjustments were made.

The Company is instructed to comply with RCW 48.05.073, RCW 48.05.250, and WAC 284-07-050(2) in filing its NAIC Annual Statements in accordance with the NAIC Accounting Practices and Procedures Manual, and the NAIC Annual Statement Instructions. The following exceptions were noted in our examination:

a. Investment in Money Market Funds

The Company's investment in Key Bank Money Market Fund was incorrectly classified as cash. This classification was not in compliance with the AP&P which requires the investments to be classified as stocks.

b. Incorrect Notes to the Financial Statements

Some of the schedules and the information disclosed in the Notes to the Financial Statements of the 2004 NAIC Annual Statement contained incorrect and/or incomplete information. Some of the errors were results of irrelevant and/or incomplete information that was caused by not updating the information from prior years' filings. Also, in several instances, the Company did not disclose all of the required information. For example, inaccurate rent income and mortgage loan information in Note No. 1. Also, the Company did not include capital stock of the reporting entity information in the investment section of general interrogatories and fair value information for short-term bonds.

c. Annual Statement Accuracy

The examination team discovered several instances in which the Company's filing of the 2004 NAIC Annual Statement did not conform to the AP&P and the NAIC Annual Statement Instructions. While the Company needs to correct these practices, these errors were not material to the financial statements and no examination adjustments were made.

2) Incorrect Inter-Company Balances

EPC recorded an incorrect cash balance for the period ended December 31, 2004. The balance was overstated by \$179,010 due to a cash transfer that was made to the parent company without the corresponding general entry in its records. At the same time, the Company recorded \$171,335 of ceded reinsurance premium payable. This amount is incorrect and the balance is the parent company's obligation rather than EPC's. The following adjustment is needed in order to correct the above errors:

	<u>DR</u>	<u>CR</u>
Ceded reinsurance premiums payable	\$171,335	
Payable to parent	7,675	
Cash		\$179,010

The Company is instructed to comply with RCW 48.05.073, RCW 48.05.250, and WAC 284-07-050(2) in filing its NAIC Annual Statements in accordance with the NAIC Accounting Practices and Procedures Manual, and the NAIC Annual Statement Instructions.

3) Administrative Service Agreement

The administrative services provided by the parent company to EPC are charged at their reasonable value, according to that agreement. However, RCW 48.31.B.030(1)(a)(iii) and SSAP No. 70, paragraph 8, requires that, "Expenses incurred and payments received must be allocated to the insurer in conformity with customary insurance accounting practices consistently applied". Therefore, the expenses must be charged on a cost basis, without any additional adjustments. The current charges are based upon data which does not demonstrate that they are purely cost-based.

The Company is instructed to work with its parent company to negotiate intercompany charges which are based on the provider's pure cost, in compliance with RCW 48.31.B.030(1)(a)(iii), and SSAP No. 70, pursuant to WAC 284-07-050(2).

COMMENTS AND RECOMMENDATIONS

None.

COMPANY PROFILE

History

The Company was incorporated on November 27, 2001, as a stock multiple line property and casualty insurer in the state of Washington. The Company commenced business in the state of Washington on January 25, 2002.

Capitalization

The Company has 300,000 outstanding shares with a par value of \$10 per share as of December 31, 2004. All of the outstanding shares are held by the parent company.

Territory and Plan of Operation

The Company was licensed in Idaho, Oregon, and Washington.

Growth of Company

The following schedules reflect the growth of the Company by year based on the NAIC Annual Statement filings beginning in 2002:

<u>Year</u>	<u>Admitted Assets</u>	<u>Liabilities</u>	<u>Capital & Surplus</u>
2004	\$ 6,703,030	\$ 212,268	\$ 6,490,762
2003	6,597,365	158,543	6,438,822
2002	6,462,836	120,770	6,342,066

<u>Year</u>	<u>Net Premium Written</u>	<u>Net Underwriting</u>	<u>Net Investment Gains (Losses)</u>	<u>Net Income</u>
2004	\$ 0	\$ 0	\$ 79,907	\$ 51,940
2003	0	(29,410)	176,011	96,757
2002	0	(9,184)	361,987	242,066

Affiliated Companies

The Company is 100% owned by its parent Mutual of Enumclaw Insurance Company (MOE). MOE, in turn, is a mutual company owned by the policyholders.

Intercompany Contracts

As of December 31, 2004, the Company was a party to the following inter-company contracts:

Administrative Services Contracts	January 25, 2001
Intercompany Quota Share Reinsurance Agreement	February 26, 2002
Consolidated Federal Income Tax Sharing Agreement	January 30, 2004

MANAGEMENT AND CONTROL

Ownership

The original authorized capital of the Company was 300,000 shares of common capital stock with a par value of \$10 per share. The Company issued one stock certificate for 300,000 shares of common capital stock to MOE in consideration for \$6,100,000. The consideration was split between paid-in capital stock for \$3 million and \$3.1 million for paid-in surplus.

All issued and outstanding shares of stock of the Company are wholly-owned by MOE.

Board of Directors (BOD)

Article III, Section 1 of the Company's Bylaws authorizes not less than seven and not more than eleven directors with whom all matters concerning the management of the

Company are vested. The BOD is comprised of nine (9) members. Elections to fill vacancies existing or occurring in the BOD are held at the annual meeting of the stockholders.

Directors of the Company as of December 31, 2004:

Directors

Vance Oswald Fredrickson
Robert Christopher Guile
Frederick Merton Schunter
Dwight Leon Cummins
Peter Charles Hanson
David Merle Waldo
Gary Philip Heer
Gerald Paul Schmidt
Bernadene Dochnahl

Officers

Officers of the Company as of December 31, 2004:

<u>Officer</u>	<u>Responsibilities</u>
Gerald Paul Schmidt	President
Frederick Merton Schunter	Treasurer
Bernadene Dochnahl	Secretary
Peter Charles Hanson	Vice President
John Robert Willis	Vice President Marketing
Eric Paul Nelson	Vice President Underwriting

Conflict of Interest

The Company does not have any employees, as it operates with the use of MOE's employees. MOE and EPC require conflict of interest statements to be completed and signed by the directors, officers, and employees for disclosure of any potential conflicts. Signed conflict of interest statements are reviewed by the BOD annually for conflicting situations.

Fidelity Bond and Other Insurance

The Company is a named insured under a financial institution bond which provides the following coverage:

<u>Type</u>	<u>Coverage Amount</u>	<u>Deductible</u>
Dishonesty:		
Employee	\$2,000,000	\$100,000
Trade or Loan	2,000,000	100,000
On Premises	2,000,000	100,000
In Transit	2,000,000	100,000
Forgery or Alteration	2,000,000	100,000
Extended Forgery	2,000,000	100,000
Counterfeit Money	2,000,000	100,000
Computer System	2,000,000	100,000

The fidelity coverage carried by the Company exceeds the minimum recommended amount by the NAIC.

Officers', Employees', and Agents' Welfare and Pension Plans

As noted under the Conflict of Interest section of this report, the Company does not have any employees, as it operates with the use of MOE's employees. As of December 31, 2004, EPC reimbursed MOE based on an inter-company sharing agreement. As such, no obligations to employees for pension or retirement plans are necessary for EPC.

CORPORATE RECORDS

The Company's BOD managed the property and business of the Company and was actively involved in the Company's affairs. Investment purchases, transfers, and disposals were ratified by the BOD and noted in the minutes. Appointments and elections of officers, reinsurance contracts, bank agreements, and other contracts were also noted in the BOD's minutes.

UNPAID LOSSES AND LOSS ADJUSTMENT EXPENSES

The reserves carried by the Company for loss and loss adjusting expenses were \$0 and \$0, respectively, as of December 31, 2004. The zero balance is accurate due to the reinsurance agreement the Company has with MOE. The agreement calls on EPC to cede 100% of its written premiums to MOE. Thus, all associated reserves are carried by MOE.

REINSURANCE

The Company cedes 100% of all business written to its parent, MOE, and is allowed a ceding commission sufficient "...to cover all underwriting and acquisition expenses..." of EPC. No other agreements were in force during the examination period under review.

STATUTORY DEPOSITS

The Company maintained the following statutory deposit as of December 31, 2004:

<u>Location</u>	<u>Type of Security</u>	<u>Par Value</u>	<u>Statement Value</u>	<u>Market Value</u>
Oregon	FNMA MTN 3% Due 8/17/2007	\$260,000	\$259,215	\$257,400

Securities held by the state of Oregon were confirmed directly with the Company's authorized custodians.

ACCOUNTING RECORDS AND INFORMATION SYSTEMS

The Company maintains its accounting records on a Generally Accepted Accounting Principles (GAAP) accrual basis of accounting and adjusts to Statutory Accounting Principles (SAP) basis for NAIC Annual Statement reporting. The Company is audited annually by the certified public accounting firm of Ernst & Young. The Company received an unqualified opinion for all years under review. The Company's accounting procedures, internal controls, and transaction cycles were reviewed during the planning and testing phase of the examination and no exceptions were noted.

The management of the Company is sufficiently knowledgeable of the information systems (IS) process. Systems development, acquisition, and maintenance controls were evaluated to gain assurance that appropriate controls are in place. Operations and application controls were reviewed to determine the type of hardware installed; operating systems and proprietary software in use; back up and recovery facilities employed; and, the controls exercised to maintain data security. Sufficient internal controls are in place and monitored by the Company. The Company's IS Department has the ability to recover from an incident or disaster and has documented these procedures in a detailed, disaster recovery plan.

SUBSEQUENT EVENTS

No material subsequent events were disclosed during the examination.

FOLLOW UP ON PREVIOUS EXAMINATION FINDINGS

This is the first full scope examination of the Company.

FINANCIAL STATEMENTS

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ENUMCLAW PROPERTY & CASUALTY INSURANCE COMPANY
ASSETS, LIABILITIES, SURPLUS AND OTHER FUNDS
DECEMBER 31, 2004

	BALANCE PER COMPANY	REF NOTE	EXAM ADJUSTMENT	BALANCE PER EXAM
Assets				
Bonds	\$ 6,259,215		\$ 0	\$ 6,259,215
Cash and short-term investments	408,024	1	(179,010)	229,014
Subtotal, cash and invested assets	<u>6,667,239</u>		<u>(179,010)</u>	<u>6,488,229</u>
Investment income due and accrued	35,791			35,791
Total Assets	<u>\$ 6,703,030</u>		<u>\$ (179,010)</u>	<u>\$ 6,524,020</u>
Liabilities, Surplus and other Funds				
Ceded reinsurance premiums payable	\$ 171,335	1	\$ (171,335)	\$ 0
Payable to parent, subsidiaries and affiliates	40,933	1	(7,675)	33,258
Total Liabilities	<u>212,268</u>		<u>(179,010)</u>	<u>33,258</u>
Common capital stock	3,000,000			3,000,000
Gross paid in and contributed surplus	3,100,000			3,100,000
Unassigned funds (surplus)	390,762			390,762
Surplus as regards policyholders	<u>6,490,762</u>		<u>0</u>	<u>6,490,762</u>
Total Liabilities, Surplus and other Funds	<u>\$ 6,703,030</u>		<u>\$ (179,010)</u>	<u>\$ 6,524,020</u>

ENUMCLAW PROPERTY & CASUALTY INSURANCE COMPANY
STATEMENT OF INCOME AND CAPITAL AND SURPLUS ACCOUNT

FOR THE YEAR ENDED DECEMBER 31, 2004

	<u>BALANCE PER COMPANY</u>	<u>REF NOTE</u>	<u>EXAM ADJUSTMENT</u>	<u>BALANCE PER EXAM</u>
STATEMENT OF INCOME				
Underwriting Income				
Premiums earned	<u>\$ 0</u>		<u>\$ 0</u>	<u>\$ 0</u>
Deductions				
Losses incurred	0			0
Loss expenses incurred	0			0
Other underwriting expenses incurred	0			0
Total underwriting deductions	<u>0</u>		<u>0</u>	<u>0</u>
Net underwriting gain or (loss)	0		0	0
Investment Income				
Net investment income earned	<u>79,907</u>		<u>0</u>	<u>79,907</u>
Net investment gain or (loss)	79,907		0	79,907
Net income, after dividends to policyholders but before federal and foreign income taxes	79,907			79,907
Federal and foreign income taxes incurred	<u>27,967</u>		<u>0</u>	<u>27,967</u>
Net income	<u><u>\$ 51,940</u></u>		<u><u>\$ 0</u></u>	<u><u>\$ 51,940</u></u>
CAPITAL AND SURPLUS ACCOUNT				
Surplus as regards policyholders, December 31 prior year	<u>\$ 6,438,822</u>		<u>\$ 0</u>	<u>\$ 6,438,822</u>
Gains and (Losses) in Surplus				
Net income	<u>51,940</u>		<u>0</u>	<u>51,940</u>
Change in surplus as regards policyholders	<u>51,940</u>		<u>0</u>	<u>51,940</u>
Surplus as regards policyholders, December 31 current year	<u><u>\$ 6,490,762</u></u>		<u><u>\$ 0</u></u>	<u><u>\$ 6,490,762</u></u>

ENUMCLAW PROPERTY & CASUALTY INSURANCE COMPANY
RECONCILIATION OF SURPLUS FOR THE PERIOD SINCE THE LAST
EXAMINATION (INCEPTION)
FOR THE YEAR ENDED DECEMBER 31, 2004

	<u>2004</u>	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>
Capital and surplus, December 31, previous year	<u>\$ 6,438,822</u>	<u>\$ 6,342,065</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
Net income	51,940	96,757	242,065	0	0
Capital changes - Paid in	0	0	3,000,000	0	0
Surplus adjustments - Paid in	0	0	3,100,000	0	0
Change in surplus as regards policyholders for the year	<u>51,940</u>	<u>96,757</u>	<u>6,342,065</u>	<u>0</u>	<u>0</u>
Surplus as regards policyholders, December 31, current year	<u>\$ 6,490,762</u>	<u>\$ 6,438,822</u>	<u>\$ 6,342,065</u>	<u>\$ 0</u>	<u>\$ 0</u>

ENUMCLAW PROPERTY & CASUALTY INSURANCE COMPANY
ANALYSIS OF CHANGES IN FINANCIAL STATEMENTS RESULTING FROM THE
EXAMINATION
AS OF DECEMBER 31, 2004

	PER COMPANY	PER EXAM	EXAMINATION ADJUSTMENT REF NOTE	INCREASE (DECREASE) IN SURPLUS	TOTAL
Capital and Surplus, December 31, 2004 - Per NAIC Annual Statement					\$ 6,490,762
<u>ASSETS</u>					
Cash	\$ 408,024	\$ 229,014	1	\$ (179,010)	
<u>LIABILITIES</u>					
Ceded reinsurance premiums payable	171,335	-	1	\$171,335	
Payable to parent, subsidiary and affiliate	40,933	33,258	1	\$7,675	
Change in surplus					0
Capital and Surplus, December 31, 2004 - Per Examination					<u>\$ 6,490,762</u>

NOTES TO THE FINANCIAL STATEMENTS

1) Cash and Inter-Company Accounts

The Company recorded an incorrect cash balance for period ended December 31, 2004. The balance was overstated by \$179,010 due to a cash transfer that was made to the parent company without the corresponding general entry in its records. At the same time, the Company recorded \$171,335 of ceded reinsurance premium payable. This amount is incorrect and the balance is the parent company's obligation rather than EPC. The following adjustment is needed in order to correct the above errors:

	<u>DR</u>	<u>CR</u>
Ceded reinsurance premiums payable	\$171,335	
Payable to parent	7,675	
Cash		\$179,010

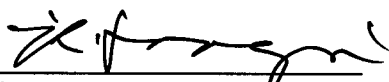
Therefore, an examination adjustment was made to correct the above errors. (See Instruction No. 2)

ACKNOWLEDGMENT

Acknowledgment is hereby made of the cooperation extended to the examination team by the officers of Enumclaw Property & Casualty Insurance Company during the course of this examination.

In addition to the undersigned, Michael V. Jordan, CPA, CFE, MHP, Assistant Chief Examiner; Tarik Subbagh, CPA, CFE, Insurance Examiner; John J. Gaynard, CPA, CFE, CPCU, Reinsurance Specialist; Timothy F. Hays, CPA, JD, Investment Specialist; Bert Karau, CPA, Insurance Examiner; Ann V. Kauffman, CPA, Insurance Examiner; Juanita M. Turley, CPA, Insurance Examiner; D. Lee Barclay, FCAS, MAAA, Senior Actuary; Eric Slavich, Actuarial Analyst; and John R. Jacobson, AFE, Automation Examination Specialist, all from the Washington State Office of the Insurance Commissioner, participated in the examination and the preparation of this report.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Timoteo L. Navaja', is written over a horizontal line.


Timoteo L. Navaja, CFE, CIE
Examiner in Charge
State of Washington

AFFIDAVIT


STATE OF WASHINGTON }
 } ss
COUNTY OF KING }

Timoteo L. Navaja, CFE, CIE, being duly sworn, deposes and says that the foregoing report subscribed by him is true to the best of his knowledge and belief.

He attests that the examination of Enumclaw Property & Casualty Insurance Company was performed in a manner consistent with the standards and procedures required or prescribed by the Washington State Office of the Insurance Commissioner and the National Association of Insurance Commissioners (NAIC).


Timoteo L. Navaja, CFE, CIE
Examiner in Charge
State of Washington

Subscribed and sworn to before me this 31st day of March, 2006.


Notary Public in and for the
State of Washington.

